

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Statutory Review of the System
for Regulating Rates and Classes
for Market Dominant Products

Docket No. RM2017-3

REPLY COMMENTS OF
PARCEL SHIPPERS ASSOCIATION (PSA)
(March 30, 2018)

Pursuant to Order No. 4258,¹ the Parcel Shippers Association respectfully submits these comments in reply to the comments of the Public Representative (PR). United Parcel Service (UPS) and the Greeting Card Association (GCA).²

UNDERWATER PRODUCT SURCHARGES

PSA joined in initial comments with the American Catalog Mailers Association (ACMA) to explain why the 2 percent non-compensatory product surcharge proposed

¹ Notice of Proposed Rulemaking for the System of Regulating Rates and Classes for Market Dominant Products, December 1, 2017 (Order No. 4258).

² See Comments of the Public Representative, March 1, 2018 (refiled March 7, 2018) (PR Comments); Comments of United Parcel Service, Inc., March 1, 2018 (UPS Comments); Initial Comments of the Greeting Card Association, March 1, 2018 (GCA Comments).

for Marketing Mail Flats (Flats) and Parcels is not warranted.³ PSA also joined with ACMA in comments replying to Valpak's initial comments in support of the surcharge for Flats.⁴

PSA submits that the same arguments against imposing a non-compensatory product surcharge for Flats apply in the case of Parcels.

A. The law does not require Marketing Mail Parcels to cover costs. The existing rates for Marketing Mail Parcels are reasonable, fair, and equitable in that they do not threaten the financial integrity of the Postal Service, and the effect of the proposed surcharges on the rates for other products would be *de minimis* at best. See 39 U.S.C. 3622(b)(8); 39 U.S.C. 101(d).

The Marketing Mail class is profitable. Thus, the factor addressing cost coverage, 39 U.S.C. 3622(c)(2), which does not apply to individual products, does not compel a surcharge for Marketing Mail generally, or individual products such as Parcels.

PSA notes the following observation of the Public Representative:

The NOPR proposes to require a 2 percent rate adjustment for classes of mail where the attributable cost for that class exceeds the revenue from that class (*i.e.*, Periodicals). Proposed 39 C.F.R. § 3010.202, NOPR, Attachment A at 25. It also proposes that for products where the attributable cost exceeds the revenue for that product (*i.e.*, currently Marketing Mail Flats and certain other products that have low revenue), the Postal Service must increase the rate for those products by 2 percent without increasing the rate allowance for the class. . . As a practical matter, *2 percent would do very little to reduce the large negative contribution of Postal Service Periodicals revenue.*

³ See Comments of the American Catalog Mailers Association and the Parcel Shippers Association, March 1, 2018 at 4-18 (ACMA PSA Comments).

⁴ See Valpak Direct Marketing Systems, Inc. and the Valpak Franchise Association, Inc. Initial Comments on the Notice of Proposed Rulemaking for the System for Regulating Rates and Classes for Market Dominant Products, March 1, 2018, (Valpak Comments).

PR Comments at 28-29 (emphasis added). The 2 percent surcharge for Marketing Mail Parcels would do even less. Existing Parcel prices do not threaten the financial integrity of the Postal Service.

Parcels make up such a small part of Marketing Mail and overall postal revenues that any effect a 2 percent surcharge may have on overall revenues would be *de minimis*, just as any “loss” under existing rates is *de minimis*.⁵ To paraphrase the Public Representative as a practical matter, 2 percent would do very little to reduce the large negative contribution of the Postal Service, period. Existing rates do not threaten the financial integrity of the Postal Service and are not unreasonable.

Similarly, the existing rate scheme for Marketing Mail Parcels is fair and equitable because its effect on rates for other market dominant rates is *de minimis*. See 39 U.S.C. 101(d).

No harm no foul.

B. The proposed Parcel surcharge is an unwarranted intrusion into the pricing flexibility supposed to be afforded to the Postal Service under the PAEA. 39 U.S.C. 3622(b)(4).

The Public Representative notes:

An additional concern is that the Commission’s attempt to direct the Postal Service to file for specific rates for specific products or classes may be construed as inconsistent with Objective 4 to allow Postal Service pricing flexibility and usurps the Postal Service’s managerial authority to propose/establish rates.

PR Comments at 30. PSA agrees. The Commission acknowledges that requiring the Postal Service to increase prices limits the Postal Service’s pricing flexibility. Order No.

⁵ According to the most recent published Cost and Revenue Analysis (Fiscal Year 2016) annual revenues for Periodicals were \$1,506.7 million; Marketing Mail class were \$17,675.1 million; and Marketing Mail Parcels were \$53.1 million. Total Market Dominant Mail revenue was \$49,039.8 million.

4258 at 77. In the recently issued Annual Compliance Determination the Commission notes the Postal Service is using the pricing flexibility afforded it to address the coverage issue in the manner it deems best, through above-average price increases.

To improve USPS Marketing Mail Parcels' cost coverage, the Postal Service states that it will continue proposing above-average price increases. FY 2017 ACR at 14. Most recently, in Docket No. R2018-1, the Commission approved a price increase for USPS Marketing Mail Parcels of 2.768 percent, 0.832 percentage points higher than the average price increase for USPS Marketing Mail of 1.936 percent. See Order No. 4215 at 37.⁶

Since the proposed 2 percent product surcharge will result in no new price cap authority it is unlikely to increase Postal Service revenue or benefit the Postal Service's financial position.⁷ This proposed intrusion into the Postal Service's pricing flexibility is unwarranted.

TREATMENT OF INSTITUTIONAL COSTS

United Parcel Service and the Greeting Card Association suggest that the existing rates and classification system for market-dominant products may not be appropriately accounting for and dividing the institutional costs of the Postal Service between market-dominant and competitive product businesses. Objective 9 provides that the system should "allocate the total institutional costs of the Postal Service appropriately between market-dominant and competitive products." 39 U.S.C. 3622(b)(9).

According to UPS:

As UPS has noted in its initial comments in this docket and in various other dockets, the United States Postal Service ("Postal Service") has built its competitive products business on the back of its market-dominant customers. The current market-dominant rate system has failed to protect against this result,

⁶ FY 2017 ACD at 62.

⁷ See ACMA PSA Comments at 10-14.

and UPS agrees with the Commission's conclusion, albeit for different reasons, that the rate system "as a whole has not achieved the objectives of the PAEA."

UPS Comments at 1.

GCA notes:

The Postal Service's competitive products have grown in both volume and contribution, and now play a major part in maintaining its financial stability. While not totally neglected in Order No. 4258, the competitive sector is reflected only through an arbitrary assumption which is not supported by analysis, ignores relevant historical results, and will predictably lead to unnecessary and unreasonable burdens on market-dominant mailers.

GCA Comments at 2.

GCA and a number of other parties suggests that future contribution from competitive products, which the Commission assumes to be static, is not appropriately taken into account. *Id.* at 2-10. This seems an appropriate inquiry but does not require any change in the existing system.

GCA also suggests how it thinks determinations relating to preventing cross subsidy under 39 U.S.C. 3633 should be approached, *Id.* at 11-18, and concludes:

The Commission should make clear in its final order in this Docket that it rejects the view that objective (b)(9) is adequately achieved if the minimum contribution share established under secs. 3633(a)(3) and 3633(b) is being provided. It should affirm, instead, that objective (b)(9) has an independent role and may be invoked to require reallocation of institutional costs between the competitive and market-dominant sectors even if that minimum share is being contributed or exceeded.

GCA Comments at 18.

PSA suggests this is better considered under proceedings under sections 39 U.S.C 3633, 3652, and 3653. There is no need for duplicative review and determination of cross-subsidy issues under objective (b)(9).

In earlier comments PSA explained why the mechanisms in place to implement Objective 9 had worked well, and urged they not be addressed in this rulemaking.⁸ But Pitney Bowes Inc. summarized it best.

The Commission properly determined that “although the mechanism for allocation is located outside of section 3622, the statutory and regulatory mechanisms to set the allocation of institutional costs required by sections 3633(a)(3) and 3633(b) provide a mechanism to appropriately allocate institutional costs between competitive and market dominant products.”

A historical review of the allocation of institutional costs between market dominant and competitive products confirms that sections 3633(a)(3) and 3633(b) have provided a workable mechanism. The Commission has conducted its review of this mechanism via open and transparent processes. The Commission’s annual compliance determinations have consistently found that collectively all competitive products are contributing more than the minimum contribution required and that competitive products are contributing an increasing share of total institutional costs each year.

Any change in this mechanism must be carefully considered to ensure that the Postal Service continues to have the flexibility to set prices for competitive products in response to market conditions. As indicated above, because the mechanism is functioning as intended and these issues are being addressed in a parallel docket, no change is appropriate as part of this proceeding.⁹

GCA also argues against elimination of the “minimum contribution requirement.” GCA Comment at 11-15. In Docket No. RM2017-1, a coalition of market-dominant mailers and competitive shippers went further:

All of us urge the Commission to eliminate the minimum contribution requirement. . . This requirement is unnecessary to promote a level playing

⁸ See Comments of the Parcel Shippers Association Pursuant to Order 3673, March 20, 2017, at 2. (“It is important to note that the PAEA specifically prohibits “cross subsidization” of competitive products. See, 39 U.S.C. 3633(a)(1) and (2). The Commission reviews this annually through the compliance process. Additionally, the Commission is in the process of reviewing the minimum contribution requirement for competitive products. See Docket No. RM2017-1. These processes have worked well, and there is no need to address this matter in the current rulemaking.”)

⁹ See Comments of Pitney Bowes Inc., March 20, 2018, at 16-17 (footnotes omitted).

field between the Postal Service and its competitors, prohibit cross subsidization, or ensure that competitive products pay an appropriate share of the Postal Service's institutional costs. Indeed, the requirement is now an irrelevant anachronism: the contribution to institutional costs earned by the Postal Service from competitive products has far outstripped the 5.5 percent minimum established in 2007. Moreover, increasing the minimum contribution requirement enough to influence competitive product prices could harm the Postal Service, its customers, and American consumers. Even leaving the required minimum contribution in place at its current level would be a needless invitation to mischief.¹⁰

In a subsequent order, Order No. 4402, the Commission made findings which PSA believes support elimination of the minimum contribution requirement:

- The minimum contribution requirement is not needed to prevent cross subsidization because the requirement that competitive product revenues exceed incremental costs already serves this purpose. *Id.* at 75.
- The minimum contribution requirement is not needed to prevent the Postal Service from sacrificing contribution to increase the scale of its operations because USPS has demonstrated no incentive to do so. Indeed, The Postal Service has substantially increased competitive contribution over the last decade. *Id.* at 75.
- The minimum contribution requirement is not needed to ensure that competitive products cover "costs [that] are uniquely or disproportionately associated with any competitive products." All of these costs are already included in competitive product attributable costs. *Id.* at 43-44.
- The minimum contribution requirement is not needed to ensure that competitive products cover fully allocated/distributed cost (FDC) because FDC costing "has long been rejected by the Commission and by economists as being inherently arbitrary." *Id.* at 81.

¹⁰ Comments of Parcel Shippers Association et al., PRC Docket No. RM2017-1 (Jan. 23, 2017) at 1-2; The parties endorsing these comments were the Parcel Shippers Association, the Alliance of Nonprofit Mailers, the American Catalog Mailers Association, the Continuity Shippers Association, the Data and Marketing Association, the Envelope Manufacturers Association, the National Association of Presort Mailers, the National Newspaper Association, PSI Systems, and Stamps.com.

But this is better addressed pursuant to the statutory and regulatory mechanisms under 39 U.S.C. 3633. So, PSA supports the Commission's finding that:

[t]he system established under section 3622 of the PAEA does not specify the amount to be allocated to market dominant products, rather it only requires that the system have a mechanism to appropriately allocate between competitive and market dominant as set forth by Objective 9. . . Based on the analysis discussed above, the Commission determines that although the mechanism for allocation is located outside of section 3622, *the statutory and regulatory mechanisms to set the allocation of institutional costs required by sections 3633(a)(3) and 3633(b) provide a mechanism to appropriately allocate institutional costs between competitive and market dominant products.*¹¹

PARALLEL TOTAL FACTOR PRODUCTIVITY FACTORS

UPS proposes that:

[T]he Commission require that Postal Service develop parallel [Total Factor Productivity (TFP)] measures for the market dominant business and the competitive products business before making TFP the basis for any performance-based market dominant rate increases. It should be a simple matter for the Postal Service to disaggregate the TFP figures for the two enterprises. It would only be necessary to replace the total labor, total capital and total material categories upon which the current TFP measure is based with figures derived from the segments and components set forth in the annual ACD filing and make a few necessary adjustments to the formula inputs.

UPS Comments at 8.

PSA disagrees that developing separate TFP figures for market dominant products and competitive products would be a simple matter. In fact, it would be impossible to do in a non-arbitrary way.

Analogous to institutional costs, a large share of the Postal Service's labor, capital, and material inputs serve both competitive and market dominant products jointly or in common and cannot be causally attributed to either.

¹¹ Order 4257 at 246-47 (emphasis added).

Replacing “the total labor, total capital and total material measures” in the TFP calculations with measures specific to the competitive and market dominant categories would require arbitrary, non-causal allocations of these inputs and should be rejected, just as the Commission has rejected non-causal attributions of institutional costs.

CONCLUSION

The Parcel Shippers Association appreciates the Commission’s consideration of these comments.

Respectfully submitted,

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